

Internal Revenue Service  
**memorandum**

CC:TL:Er3  
GEBowden

date: NOV 9 1987

to: District Counsel, San Jose W:SJ

from: Acting Director, Tax Litigation Division CC:TL

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subject: [REDACTED]  
Request for Technical Advice

A memorandum from your Special Trial Attorney, Ray Collins, dated September 21, 1987, requested Technical Advice.

ISSUES

Whether I.R.C. § 6622 requires the compounding of interest on simple interest that accrued on proposed deficiencies prior to January 1, 1983. Whether the Tax Court has jurisdiction to resolve this question in the instant case.

CONCLUSION

The compounding rules of § 6622 apply to simple interest accrued but unpaid prior to January 1, 1983. The Tax Court has no jurisdiction to address these issues in the instant case.

FACTS

The federal income tax liabilities of [REDACTED] for its [REDACTED] and [REDACTED] tax years are presently pending in the Tax Court awaiting a final opinion on one of the issues litigated in [REDACTED]. The deficiencies are: [REDACTED]-\$[REDACTED] and [REDACTED]-\$[REDACTED]. The Court chose to issue a series of separate opinions on the [REDACTED] issues litigated. [REDACTED] opinions have been issued to date and a [REDACTED] is pending. According to calculations prepared by petitioner, respondent has been sustained on at least \$[REDACTED] of the alleged [REDACTED] proposed deficiencies.

In [REDACTED], petitioner elected to take advantage of certain provisions in IRS Announcement 86-108. On [REDACTED], petitioner proffered a check in the amount of \$[REDACTED]. In their letter, petitioner designated \$[REDACTED] of the amount tendered as a partial payment of income tax for the [REDACTED] tax year and \$[REDACTED] as interest on the income tax. Mr. Collins' letter in response merely

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accepted the tendered amount on behalf of the IRS, but took no position on the correctness of the designations.

In a letter dated [REDACTED] petitioner's counsel pleaded that they made an error when they calculated the interest due on \$ [REDACTED] and asked the IRS to refund \$ [REDACTED]. Petitioner has filed a claim for refund. Petitioner's counsel also proposes to amend the Petition and ask the Tax Court to grant relief if the IRS does not refund the alleged overpayment of interest. Petitioner's explanation of this "error" is that when it computed the interest due on the \$ [REDACTED] they compounded interest starting [REDACTED] on the simple interest that had accrued between [REDACTED] and that date. This approach, petitioner maintains, although in conformance with Reg. Section 301.6622-1(c), is contrary to the express provisions of Section 344 P.L. 97-248 (TEFRA) which enacted § 6622. Thus, petitioner maintains that the regulation is invalid and that an overpayment of interest has been made.

A similar situation exists with respect to petitioner's subsidiary, [REDACTED]. Here, petitioner and respondent reached partial agreement on deficiencies for tax years [REDACTED] and [REDACTED]. In [REDACTED], petitioner paid the agreed deficiencies as well as the interest accrued thereon as computed by the IRS. Petitioner raises the same argument and has filed a claim for refund in the amounts of \$ [REDACTED] and \$ [REDACTED] for [REDACTED] and [REDACTED] respectively.

#### ANALYSIS

The position of the Internal Revenue Service on the first issue is clear. Treas. Reg. § 301.6622-1(c) provides:

(c) Applicability to unpaid amounts on December 31, 1982 - (1) In general - The unpaid interest (or other amount) that shall be compounded daily includes the interest (or other amount) accrued but unpaid on December 31, 1982.  
(emphasis added)

See also Treas. Reg. § 301.6601(f)(2). This position is also set forth in Rev. Proc. 83-7, 1983-1 C.B. 583, section 3.02 which provides:

Interest on tax and penalty outstanding as of December 31, 1982 will be computed in accordance with section 3.01. (using tables) At that time, all tax, assessed penalty or addition to tax, and interest (whether or not assessed) will be added together to determine the amount to be carried over on which daily interest will be charged under the compounding rules.

Petitioner's contention that this position is in conflict with § 344 of TEFRA is apparently based on its interpretation of § 344(c) which provides for the effective date of the modification as follows: "[t]he amendments made by this section shall apply to all interest accruing after December 31, 1982." Despite the fact that the subsection is entitled "effective date" petitioner apparently believes that this section limits the amounts subject to compound interest to those accruing after December 31, 1982. This rather tortured reading of the statute is contrary to the intent of Congress as revealed in the legislative history.

Explicit support for the IRS position is provided by the Committee Conference Report which accompanied TEFRA:

This compounding requirement would apply to interest accruing after December 31, 1982, on amounts (including interest) remaining unpaid after that date.  
(emphasis added)

H. Rep. No. 97-760 (August 17, 1982), p. 596 (Joint Explanatory Statement of Committee of Conference).

Further support is provided by the comments of the Staff of the Joint Committee on Taxation in the General Explanation of the Revenue Provisions of the Tax Equity and Fiscal Responsibility Act of 1982, dated December 31, 1982, which read:

This compounding requirement applies in determining interest after December 31, 1982 on any amount, whether principal or interest, owing on or after January 1, 1983.  
(emphasis added)

Although the Senate Finance Committee report does not make any reference to this issue, the IRS position is entirely consistent with the reason for the change set forth by the Committee. The explanation of the provision by the Senate Finance Committee is as follows:

Under the Committee bill, all interest payable under the internal revenue laws will be compounded daily. This adjustment will conform computation of interest under the internal revenue laws to commercial practice. The change will also offset any other amounts computed by reference to the interest rate provided for in the code.

It seems more reasonable that interest on all amounts owing as of December 31, 1982 should conform with commercial practice than that only those amounts attributable to tax and penalties should be brought into conformance.

Because § 6601(e)(2), which prohibited interest accruing on interest, was repealed effective for interest accruing after December 31, 1982, there is nothing in the Code which prevents post-1982 compound interest from being computed with reference to the amount of unpaid pre-1983 interest. Charging compound interest on unpaid pre-1983 interest furthers the enforcement policy of TEFRA by reducing the incentive to prolong tax matters. It would also eliminate the tactic of paying a deficiency (but not the accrued interest or penalty) to prevent the further accrual of interest.

A final argument supporting the Service's position is based on the well settled rule of statutory construction that where an administrative construction of a statute has been followed by Congressional reenactment without change, a presumption is created that Congress approved such construction. Here, the Service has taken a clear and consistent position with respect to its construction of the section in its regulations, procedures and practices and its impact has been felt by almost every taxpayer who had a deficiency or was owed a refund by the Government for a tax year prior to 1982 which was unpaid on or after December 31, 1982. Congress has not at any time since the enactment of the section, through the Tax Reform Act of 1986, expressed dissatisfaction with the Service's construction.

There are no reported decisions on this issue. There is one case currently before the Claims Court, Gannet v. United States, Docket No. 476-86T, which deals with precisely this issue. Oral argument is scheduled for November 24, 1987.

We turn now to the second question, whether the Tax Court has jurisdiction to decide this question in the instant cases. The Court's jurisdiction is limited by statute, I.R.C. § 7442. Specific statutory authority to deal with interest is limited to jeopardy assessments (§ 6861(c)) and transferee liability (§ 6901). Courts have consistently held that the Tax Court ordinarily has no jurisdiction over interest: Standard Oil Co. v. McMahon, 244 F.2d 11 (2d Cir. 1957); Commissioner v. Kilpatrick's Estate, 140 F.2d 887 (6th Cir. 1944); LTV Corp. v. Commissioner, 64 T.C. 589 (1975); and most recently Commissioner v. McCoy, \_\_\_ U.S. \_\_\_, No. 87-75 (October 19, 1987). Clearly, jeopardy assessments and transferee liability are not relevant to this case.

In this case petitioner asserts in amended petitions that there is an overpayment. When an overpayment exists the Tax Court has found that it has jurisdiction to determine the appropriate amount of interest, as long as the IRS had originally determined that there was a deficiency, Estate of Baumgardner v. Commissioner, 85 T.C. 445 (1985). Overpayment

jurisdiction is provided by § 6512. Although "overpayment" is not defined in the statute, the Tax Court cited with favor in this context the Government interpretation provided by Treas. Reg. § 301.6611-1(b). Judge v. Commissioner, 88 T.C. No. 66 (1987). The regulation provides:

. . . there can be no overpayment of tax until the entire tax liability has been satisfied. Therefore, the dates of overpayment of any tax are the date of payment of the first amount which (when added to the previous payments) is in excess of the tax liability (including any interest, addition to the tax, or additional amount) . . .

In the [REDACTED] case, then, there is no overpayment since the petitioner apparently concedes that its deficiency, independent of interest, for tax year [REDACTED] is at least \$ [REDACTED] and petitioner has made payment of \$ [REDACTED] designated for that deficiency. Even granting that petitioner's approach to the calculation of interest is correct, its total liability, including interest, must have exceeded \$ [REDACTED] for [REDACTED] as of its payment date of [REDACTED]. Petitioner made payment of a total of \$ [REDACTED] on that date, which clearly was insufficient to constitute an overpayment. So the Tax Court would have no jurisdiction to decide this question with respect to the [REDACTED] litigation.

As to the [REDACTED] case, petitioner has paid in full the taxes plus interest resulting from a partial agreement. Since this is described as a "partial" agreement, we may assume that there exist additional unpaid amounts and thus no overpayment exists. Thus there is no Tax Court jurisdiction to determine interest.

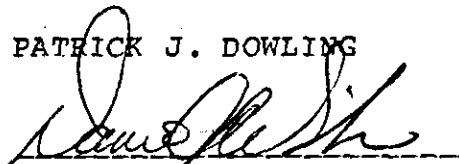
In sum then, the Tax Court does not presently have the jurisdiction to address this issue in these cases. Should an overpayment be made then the Court would, under the Baumgardner rationale, have jurisdiction to decide the issue. A provision in the Senate version of the Taxpayer's Bill of Rights would give the Tax Court jurisdiction to reopen cases where the taxpayer has fully paid the deficiency and interest claimed by the IRS to determine whether there has been an overpayment. This serves to buttress the conclusion that there is presently no jurisdiction, since otherwise the Senate would not need to create it. Still, this does create the prospect that in the instant cases the taxpayer may be able to have the Tax Court address the issue should the provision become law.

As to the more substantive first issue, the IRS position is clearly spelled out in regulations and revenue rulings. The compounding of interest does apply to simple interest that had

accrued but remained unpaid as of January 1, 1983. This interpretation is not in conflict with the language of the statute, is expressly supported by the legislative history, and comports with the statutory intent of improved compliance.

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